# Air Resources Board

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May 30, 2007

Ms. Gloria D. Smith
Mr. Brent Newell
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South San Francisco, California 94080-7037

Dear Ms. Smith and Mr. Newell:

The Office of Legal Affairs of the Air Resources Board (ARB or Board) has completed its review of your petition, dated January 13, 2006, requesting ARB to conduct a public hearing to review certain December 15, 2005 amendments adopted by the San Joaquin Valley Unified Air Pollution Control District (SJVUAPCD or District) to its Rule 2201, "New and Modified Stationary Source Review Rule." Your Petition claims that two elements of the amendments constitute impermissible weakenings of the District's new source review (NSR) rule. One amendment removes from the requirement for certification of statewide compliance those modifications that are major modifications under the regulation but are no longer federal major modifications. The other amendments affect Rule 2201, section 7, "Annual Offset Equivalency Demonstration and Pre-baseline ERC Cap Tracking System." Amendments to NSR rules that make them less stringent than the rule as it existed on December 30, 2002, are generally prohibited by Senate Bill 288 (Stats 2003 ch 476, Sher), the Protect California Air Act of 2003, which enacted Health and Safety Code (HSC) sections 42500-42507.

As enacted by SB 288, HSC section 42504(a) establishes a mechanism under which ARB may conduct a hearing to review whether a district's amendments to its NSR rule meet SB 288 criteria. There are no provisions for petitions requesting ARB to conduct a HSC section 42504(a) hearing to review a district's NSR rule amendments. As discussed below, I have concluded that at present the challenged amendments, in the context of the District's overall December 15, 2005 NSR amendments, have no or a de minimis adverse impact on the stringency of the regulation and therefore do not trigger the need for an ARB hearing. If such a hearing were to be conducted, based on the information we have received I would recommend that the amendments not be found inconsistent with the SB 288 criteria. Nevertheless, if you wish we are prepared in this particular instance to schedule a hearing by our Board at which you could present the

basis for your position that the Board should find that adoption of the amendments violated SB 288.

## The Challenged Amendments to the District's Rule 2201

Federal NSR regulates the construction and modification of sources that result in significant increases in emissions of air pollutants such as volatile organic compounds, oxides of nitrogen, and particulate matter. Along with requiring the use of highly effective emission controls by the new or modified source, federal NSR requires that all new emissions from the source be offset by emission reductions from other sources in the area. On December 15, 2005, the District adopted a range of amendments to its NSR rule, Rule 2201. Most of the amendments were designed to meet U.S. Environmental Protection Agency (U.S. EPA) requirements under what are called the federal NSR reforms promulgated by U.S. EPA December 31, 2002 (67 F.R. 80185). Your Petition challenges the following two elements of these amendments.

### Certification of Statewide Compliance

Before the amendments, section 4.15 of Rule 2201 required that the owner of any proposed new major source or major modification demonstrate (typically by certification) that all major stationary sources it owns in the State "are in compliance or on a schedule for compliance with all applicable emission limitations and standards." The December 15, 2005 amendments changed "major modification" to "federal major modification." The effect of this amendment is that projects that were "major modifications" under the federal NSR Rules as of December 30, 2002 – but would not be "major modifications" under the federal NSR reforms promulgated by U.S. EPA December 31, 2002 – were no longer required to provide the certification of statewide compliance.

Your Petition identifies instances in which the NSR reforms have the effect of excluding modifications from the federal major modification category, specifically modifications that are subject to a plantwide applicability limit or those allowed to use the pre- and post-project emissions pursuant to 40 CFR Part 51.165(a)(1)(xxviii) and 40 CFR Part 51.165(a)(1)(XXXV)(A) through (D). You indicate that the District's amendment eliminates the statewide certification "requirement" for an untold number of projects and will allow illegal emissions to continue even though the prior rule provided a means to eliminate those excess emissions.

**Annual Offset Equivalency Demonstration and Pre-baseline ERC Tracking System**

Rule 2201 section 7, "Annual Offset Equivalency Demonstration and Pre-baseline ERC Cap Tracking System," resulted from a disagreement between the District and U.S. EPA about whether federal law required the District's NSR rule to contain a "surplus-at-time-of-use" requirement under which the surplus value of emission reduction credits are determined at the time they are to be used as opposed to the time they were generated. The District took the position that failure to include a "surplus-at-time-of-use" provision did not cause the District offset rules to be less stringent than the federal requirements because other more stringent elements in the District's rule meant that the District's offsets requirements overall will achieve at least as many surplus-at-time-of-use emission reductions as the federal regulations.

This issue was ultimately addressed by the addition of section 7, which essentially required the District each year to track the quantity of offsets that would have been required for major new sources and major modifications had the federal NSR regulations in effect on December 19, 2002 applied to these sources. December 19, 2002 is the date the District amended section 7 to make it fully acceptable to U.S. EPA. In tracking offsets under the federal scenario, the District was directed to include offsets using actual emissions baselines when required under the December 19, 2002 version of the applicable federal regulation. These tracking requirements were contained in section 7.1.1. Section 7.2 directed the District to release an annual report comparing the annual quantity of federal offsets that would have been required (based on the tracking) to the quantity of offsets actually required under the rule. Section 7 also specifies actions the District must take to remedy any emission offset shortfalls. Under section 7.4.1.1, the District is required to retire additional creditable emission reductions to satisfy any shortfall. If the District does not have sufficient additional creditable emission reductions, all Authorities to Construct issued after the report deadline for that year had to comply with the federal offset requirements in effect December 19, 2002, until the NSR Rule was revised to comply with the Federal NSR requirements and approved into the State Implementation Plan by U.S. EPA. In the four years since the Offsets Equivalency Demonstration provisions have been in effect, there has never been a shortfall in federal offsets.

Your Petition focuses on the District's amendments to section 7 deleting the references to the federal NSR requirements "in effect December 19, 2002" – a date preceding U.S. EPA's December 31, 2002 promulgation of the NSR reforms that allowed more types of modifications to escape the federal NSR requirements. One District amendment deleted the references to "in effect December 19, 2002" in the section 7.1.1 provisions on tracking the quantity of offsets under the federal scenario. The other amendment deleted the references to "in effect December 19, 2002" in the remedies

provisions of section 7.4.1.2. Thus the effect of the amendments is that in tracking offsets under the federal scenario as part of the equivalency demonstration, the District will no longer have to account for federal offsets that would have been required under the federal NSR requirements in effect December 19, 2002, but are not required under the federal NSR requirements in effect now.

Although your Petition does not mention it, the December 15, 2005 amendments to section 7.1.1 also changed the reference to the type of major modifications that are included in the District's annual tracking exercise identifying the quantity of offsets required under the federal scenario. The Rule had required the tracking exercise for all "major modifications." The amendments changed the reference to "federal major modifications." This had the effect of eliminating from the tracking exercise any modifications that were "major modifications" under the federal NSR requirements before the NSR reforms, but are not "major modifications" under the current NSR requirements.

**The Requirements of SB 288**

The key SB 288 restrictions on districts amending their NSR rules are contained in the four subsections of HSC section 42504.

HSC section 42504(a) provides:

> No air quality management district or air pollution control district may amend or revise its new source review rules or regulations to be less stringent than those that existed on December 30, 2002. If the state board finds, after a public hearing, that a district's rules or regulations are not equivalent to or more stringent than the rules or regulations that existed on December 30, 2002, the state board shall promptly adopt for that district the rules or regulations that may be necessary to establish equivalency, consistent with subdivision (b).

This provision sets forth an overall equivalency requirement that allows a district to relax one NSR element only as long as one or more other elements are sufficiently strengthened to result in overall equivalent stringency. We interpret this broadly-worded provision to include offset requirements and to apply on a programmatic basis. For example, a district would not be allowed to relax NSR offset requirements if the overall effect of the district's amendments would render the NSR rules less stringent in the aggregate.

HSC section 42504(b) supplements this general prohibition against weakening NSR rules and regulations by delineating four elements which cannot be revised if the revisions would "exempt, relax, or reduce the obligations of a stationary source. . . . " These elements are listed in HSC section 42504(b)(1):

> (A) The applicability determination for new source review.
>
> (B) The definition of modification, major modification, routine maintenance, or repair or replacement.
>
> (C) The calculation methodology, thresholds or other procedures of new source review.
>
> (D) Any definitions or requirements of the new source review regulations.

HSC section 42504(b)(2) provides that the rule components listed above may not be amended if doing so would "exempt, relax, or reduce the obligations of a source" with regard to the following requirements:

> (A) Any requirements to obtain new source review or other permits to construct, prior to commencement of construction.
>
> (B) Any requirements for best available control technology (BACT).
>
> (C) Any requirements for air quality impact analysis.
>
> (D) Any requirements for recordkeeping, monitoring and reporting in a manner that would make recordkeeping, monitoring, or reporting less representative, enforceable, or publicly accessible.
>
> (E) Any requirements for regulating any air pollutant covered by the new source review rules and regulations.
>
> (F) Any requirements for public participation, including a public comment period, public notification, public hearing, or other opportunities or forms of public participation, prior to issuance of permits to construct.

HSC section 42504(c) provides,

> In amending or revising its new source review rules or regulations, a district may change any of the items in paragraph (1) of subdivision (b)

only if the change is more stringent than the new source review rules or regulations that existed on December 30, 2002.

Finally, notwithstanding the general anti-backsliding provision set forth in HSC section 42504(a) and the source-specific prohibitions set forth in HSC section 42504(b), SB 288 allows revisions that may result in less stringent district NSR rules under the carefully circumscribed circumstances described in HSC section 42504(d). The rule amendment must be accomplished at a public hearing based upon substantial evidence in the record and the district must submit the amendment(s) to the ARB for approval at a public hearing in order to ensure that the several conditions for such rule revisions have been met. Since the SJVUAPCD has not attempted to invoke HSC section 42504(d) with respect to the amendments covered by your petition, I do not list the conditions here.

## Applying SB 288 to the Challenged Amendments to Rule 2201

We have reviewed your claim that the changes to the District rule are governed by the provisions of HSC section 42504(b). Specifically, you state that the challenged amendments fall under HSC section 42504(b)'s mandate that a district may not exempt, relax or reduce "any requirement to obtain new source review or other permits to construct, prior to commencement of construction," citing HSC section 42504(b)(2)(A). But the amendments to Rule 2201 do not change the requirements that sources undergo "new source review" and obtain permits prior to construction and, as such, do not fall within the constraints of 42504(b). While projects that are "major modifications" but not "federal major modifications" will no longer be required to provide a certification of statewide compliance and will not be factored into the annual offset equivalency demonstration, they <u>will</u> still be required to obtain NSR permits from the District and to provide offsets. Therefore, ARB staff reviewed the challenged amendments to the District's NSR rule to determine if the program was weakened as a whole, as provided by section 42504(a).

### Certification of Statewide Compliance

Concerning the requirement for statewide compliance certification, we find that this change represents a *de minimis* weakening. Staff research indicates this requirement rarely impedes air district action on an application for an authority to construct and is essentially administrative in nature. The requirement states that a facility must certify that "all stationary sources owned or operated by such person (or by an entity controlling, or controlled by, or under common control with, such person) in California which are subject to emission limitations are in compliance <u>or are on a schedule of compliance</u> with all applicable emission limitations and standards." (emphasis added). ARB staff finds that when this requirement would be applied to sources that may be out

of compliance with rules affecting emissions, the source has corrected the noncompliance or has obtained a variance from the district. The economic and punitive disincentives to noncompliance ensure this outcome. Therefore, the sources are almost universally in compliance with emission limits or subject to a schedule of compliance. In addition, these same sources are required to certify compliance once a year under the federal Title V program.

**Annual Offset Equivalency Demonstration and Pre-baseline ERC Tracking System**

Your Petition asserts that the District's amendments deleting the reference in section 7 to NSR rules "in effect on December 19, 2002" mean that "it will now be much easier for the District to show that the [District and federal] programs are equivalent because the relaxed federal rules will require fewer creditable offsets." (Petition at 11.) You do not, however, identify any specific elements of the federal NSR reform amendments that in fact lessen the number or nature of creditable offsets required under the federal program. ARB staff has carefully reviewed the NSR Reform amendments and has concluded that almost all of the impacts regarding offsets would come from amendments discussed above that exclude some major modifications from the "federal major modification" category. Therefore, in evaluating the actual impact of the amendments to section 7, staff has focused on the change to the characterization of a "major modification" under federal NSR.

To assess the potential impact of the amendments on emissions, staff reviewed past permitting activities of the District assuming the District's amendments were already in effect during the four-year period when the District has been required to track emission offsets for federal equivalency. First, since the amendments only affect the treatment of "major modifications" under the District's NSR rule, staff determined how many major modifications have been processed by the District. Staff found that over the four-year period, the District processed approximately 9,360 projects and issued 16,208 Authorities to Construct (ATC). Of the 9,360 projects over the four-year period, <u>only four were major modifications</u>. All of the other ATCs issued were either for new sources – which were not affected by the NSR reform amendments – or for modifications to existing sources that did not increase emissions by more than the preexisting major modification thresholds (50,000 lbs. per year for NOx and VOC; 30,000 lbs. per year for PM10; and 80,000 lbs. per year for SOx).

Second, before <u>any</u> project's offsetting requirements would be affected by a change in the treatment of the four major modifications due to the District's challenged amendments, the District would have to fail its annual offset equivalency demonstration. This has not happened in the four years the equivalency program has been in effect, and a worst-case treatment of the offsets for the four major modifications during the

period (assuming that none of the offsets were surplus at time of use) would not have caused the District to fail the equivalency demonstration for any year. For this reason, applying the amendments to the first four years of the equivalency demonstration program would not have had any adverse emissions impact.

Third, of the four major modifications analyzed, three of the projects supplied credits that were entirely surplus at the time of use. Therefore, excluding these three projects from the equivalency tracking system due to the amendments to section 7 would have no impact on the District's equivalency demonstration.

Fourth, the only offsets supplied by the one remaining major modification that were not surplus at the time of use were SOx credits. Surplus SOx credits are relatively plentiful in the District, and had the project needed SOx credits that were surplus at the time of use they could have been readily obtained.

This analysis is necessarily based on past activity in the District. Although it can be a good predictor of the future, it is always possible that the impact of the amendments could be different in the coming years. ARB staff will continue to monitor the District's tracking system under these provisions to ensure that the emission impacts of these rule changes remain *de minimis*.

ARB staff also considered whether any other amendments to Rule 2201 adopted by the District on December 15, 2005 might have increased the Rule's stringency. By adding section 4.2.3.5, the District eliminated the exemption from best available control technology for federal major modifications that are being modified solely for the purpose of compliance with requirements of District, state, or federal air pollution controls laws, regulations, or orders. Again, as in the offset tracking discussion above, any attempt to quantify the benefit is necessarily hypothetical. Nevertheless, ARB staff believes there will be cases where elimination of this exemption will result in an emissions benefit, and any such emission benefits would have to be taken into account in determining whether the amendments to section 7 render the District's NSR rule not equivalent or more stringent than it was as it existed on December 30, 2002. This reinforces our view that the December 15, 2005 amendments to Rule 2201 did not render the Rule less stringent than it was before.

## Conclusion

After considering the effect of the challenged amendments, I have concluded that they do not cause the District's NSR rule to be less stringent than the rule was on December 30, 2002. Consequently, should a public hearing before our Board occur on

this matter, based on the information now before me I would recommend that the Board not make a finding on non-equivalency.

Notwithstanding my conclusions, we are prepared in this particular instance to schedule a hearing by the ARB Governing Board hearing on your Petition if you so desire. Please let us know if you want to pursue that course of action. In the meantime, you have any questions about ARB's legal analysis please contact me at (916) 323-9606 or Ms. Leslie Krinsk, Senior Staff Counsel at (805) 473-7325. For technical questions about the District's NSR rule, please contact Mr. Chris Gallenstein, Staff Air Pollution Specialist in the Stationary Source Division at (916) 324-8017.

Sincerely,

/s/

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Chief Counsel

cc: See next page.

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